Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
Lifeline and Link Up	)	WC Docket No. 03-109
	)	
Universal Service Contribution Methodology	)	WC Docket No. 06-122
	)	
Numbering Resource Optimization	)	CC Docket No. 99-200
	)	
Implementation of the Local Competition	)	
Provisions in the Telecommunications Act of	)	CC Docket No. 96-98
1996	)	
	)	
Developing a Unified Intercarrier	)	CC Docket No. 01-92
Compensation Regime	)	
	)	
Intercarrier Compensation for ISP-Bound	)	CC Docket No. 99-68
Traffic	)	
	)	
IP-Enabled Services	)	WC Docket No. 04-36

REPLY COMMENTS OF THE NEW JERSEY DIVISION OF RATE COUNSEL

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I. INTRODUCTION

A. TIME FRAME

The rushed comment cycle should not lead to hasty decision-making.

Dozens of entities collectively filed thousands of pages the day before Thanksgiving on matters of great significance to residential consumers and business consumers throughout the country and on complex issues that have challenged the Federal Communications Commission ("FCC" or "Commission") for many years.[1] Initial comments express concern about the hurried reform that the Commission seemingly is intent on pursuing and urge the Commission instead to allow sufficient time and opportunity for meaningful analysis and comment.[2] The Commission granted an extension of time to file reply comments the day before reply comments were originally due, citing the volume of initial comments, the intervening holiday, and the complexity of the issues.[3] New Jersey Division of Rate Counsel ("Rate Counsel") respectfully disagrees with the Commission's assertion that the *Order and FNPRM*[4] upon which the Commission seeks comment contains proposals and matters "that have been extensively briefed by interested parties since these proceedings began."[5]

The present market, in which different intercarrier compensation ("ICC") rates exist, distorts investment and purchasing decisions.[6] The universal service fund ("USF")

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[1] / Rate Counsel's lack of reply to any specific comments does not imply support. Rate Counsel reviewed a subset of the dozens of comments that were submitted.

[2] / *See, e.g.*, California Public Utilities Commission ("CPUC"), at 2; Washington Utilities and Transportation Commission ("WUTC"), at 2-3; National Association of Regulatory Utility Commissioners ("NARUC"), at 3.

[3] / *In the Matter of High-Cost Universal Service Support et al.*, WC Docket Nos. 05-337 et al., *Order*, DA 08-2631, rel. December 2, 2008. NARUC's position that a 90-day comment cycle for such a complex proposal (much less three proposals) is more appropriate to allow for review, analysis, and support of the Commission's ultimate findings is correct. NARUC, at 3. Last minute "reprieves" should not be substituted for an established, predictable timeline for analysis and input from the outset.

[4] / *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service; Lifeline and Link Up; Universal Service Contribution Methodology; Numbering Resource Optimization; Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Developing a Unified Intercarrier Compensation Regime; Intercarrier Compensation for ISP-Bound Traffic; IP-Enabled Services*, CC Docket Nos. 96-45, 96-98, 99-68, 99-200, 01-92, WC Docket Nos. 03-109, 04-36, 05-337, 06-122, Order on Remand and Report and Order ("Report and Order") and Further Notice of Proposed Rulemaking ("FNPRM"), FCC 08-262 (rel. Nov. 5, 2008).

[5] / *In the Matter of High-Cost Universal Service Support et al.*, WC Docket Nos. 05-337 et al., *Order*, DA 08-2631, rel. December 2, 2008, at para. 3.

[6] / AdHoc Telecommunications Users Committee ("AdHoc"), at 2.

is long overdue for reform. Market imperfections continue to thwart the availability of affordable broadband throughout the nation. Yet initial comments show widespread concern that the FCC's proposals for reforming intercarrier compensation, the USF, and broadband support would create ambiguity,[7] are unlawful,[8] and are arbitrary and capricious.[9]

B. LACK OF DATA

Comprehensive supporting data and cost studies should be available to inform intercarrier compensation and universal service reform.

Others echo Rate Counsel's concern about the lack of cost studies, and lack of supporting information for the diverse proposals.[10] Rate Counsel concurs with Broadview's assessment that additional proceedings are needed to examine the impacts of various proposals on the industry and to assess other alternative proposals.[11]

C. SUMMARY OF COMMENTS

Although the FCC's proposals for reform are deeply flawed, there are some salvageable components. The FCC should move forward on the following aspects of its proposal:

- Implementing signaling requirements to prevent phantom traffic;
- Eliminating the identical support rule; and

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7 / *See, e.g.*, COMPTEL, at 2 (indicating that "the three Appendices are fraught with ambiguities").

8 / *See, e.g.*, Massachusetts Department of Telecommunications and Cable ("MDTC"), at 8; COMPTEL, at 6-10; Broadview Networks, Cavalier Communications, Nuvox Inc., Pac-West Telecomm, Inc., tw telecom inc., XO Communications ("Broadview, *et al.*"), at 3, 16-29; National Association of State Utility Consumer Advocates, Maine Office of Public Advocate, Maryland Office of Peoples' Counsel, The Utility Reform Network, and the Utility Consumer Action Network ("NASUCA, *et al.*"), at 8-9; NARUC, at 6-11.

9 / Embarq, at 3.

10 / *See, e.g.*, MDTC, at 3, 19-20; Embarq, at 18 (stating "there is no support provided at all for the decision to assess the specific amount of $1.00 per number").

11 / Broadview, *et al.*, at 15-16.

- Establishing broadband subsidies for Lifeline customers, but with certain improvements relative to the FCC's plans.

Other aspects of the FCC's proposals are fundamentally flawed such as:

- Increasing the interstate subscriber line charge ("SLC") caps;
- Adopting an ill-conceived marginal cost standard;
- Unlawfully pre-empting state rate-making authority;
- Erroneously classifying voice over Internet protocol ("VoIP") as an information service;
- Including excessive opportunities for "revenue recovery" from ratepayers;
- Blending high cost and broadband support rather than establishing a separate broadband fund; and
- Changing the present revenue-based universal service fund contribution system to a numbers-based system.

Rate Counsel welcomes the opportunity to contribute to future dialogue about how best to achieve intercarrier compensation and universal service reform, and specifically to ways in which the reform can lead to consumer benefit and the furtherance of the public interest. Rate Counsel also welcomes the opportunity to continue its participation in the national dialogue about how best to achieve the universal deployment of affordable broadband. Rate Counsel reiterates its recommendation that the Commission consider the option of addressing these issues through a negotiated rulemaking, as permitted under section 561 *et seq,* of the Negotiated Rulemaking Act ("the Act"), consistent with section 553 of Title 5 of the Administrative Procedure Act. Section 563 of the Act permits an agency *to* "...establish a negotiated rulemaking committee to negotiate and develop a proposed rule, if the head of the agency determines that the use of the negotiated rulemaking procedure is in the public interest."[12] A negotiated rulemaking process would ensure not only the balanced representation of the issues but also of all who would be significantly affected by the proposed rulemaking.

II. IMPACT OF REFORM ON CONSUMERS

Initial comments do not alter Rate Counsel's initial conclusion that the FCC's proposals would yield far greater consumer harm than consumer benefit.

The initial comments do little to assuage Rate Counsel's concern[13] that under the contemplated proposals, the total new annual cost to consumers of intercarrier compensation reform would be approximately $2.8 billion in subscriber line charges.[14] These proposed increases are not cost-justified, and, furthermore, would not be balanced by commensurate consumer benefit. Instead, additional significant costs would be associated with the proposed erroneous classification of VoIP as an information service, which would, among other things, lead to the loss of consumer protection that state regulation affords. Offsetting these significant costs would be only a potential offsetting benefit: a flow-through of reduced switched access charges in retail rates. However, such a flow-through is unlikely to occur.[15] The California Public Utilities Commission ("CPUC") "urges the Commission to require interexchange carriers to pass through to their subscribers any savings from the reductions in terminating access charges" and further states that "[i]f these carriers are not required to pass through these savings, then

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12 / Negotiated Rulemaking Act, 5 U.S.C. § 563 *et seq.*

13 / Rate Counsel, at 7.

14 / *See id.*, at footnotes 18 through 20 for calculation of consumer cost. This includes $1,543,590,000 for residential and single-line business lines; $173,880,000 for non-primary residential lines; and $1,089,951,600 for multi-line business lines.

15 / *See* Rate Counsel initial and reply comments regarding the Missoula Plan, filed October 25, 2006 and February 1, 2007, for a discussion of this point.

the amount saved should at least be deducted from any revenue loss figures."[16] The Washington Utilities and Transportation Commission ("WUTC") similarly expresses concern that access charge reductions will not be passed on to consumers and urges the Commission to develop a "mechanism to assure adequate flow-through of the access charge reductions to retail consumers."[17] Rate Counsel does not share AT&T's optimism about carriers flowing through their reduced intercarrier compensation costs.[18] Instead, increasing market concentration and the evolving telecommunications/cable duopoly make it unlikely that consumers will benefit from ICC reform, as it is proposed by the FCC.

Similarly, the proposed reform to universal service would yield significant consumer costs. The proposals would further entrench the flawed high cost fund by linking it to broadband deployment. Also, the high-cost fund would continue to over-subsidize many carriers in perpetuity. The potential benefits of the expansion of broadband deployment and the proposed Broadband Lifeline Pilot Program do not adequately compensate consumers for these costs.

Rate Counsel reiterates its long-standing opposition to the use of the USF as a way to offset foregone access charge revenues.[19] Among other things, as the National Association of State Utility Consumer Advocates, Maine Office of Public Advocate, Maryland Office of Peoples' Counsel, the Utility Reform Network, and the Utility Consumer Action Network ("NASUCA, *et al.*") observe, the FCC's proposals fail to

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16/ CPUC, at 16.

17/ WUTC, at 8.

18/ AT&T, at 18-21.

19/ *See* NASUCA, *et al.*, at 21-23 (discussing the proposed "new" universal service support that would be awarded to rate-of-return carriers and to price-cap carriers based on different standards).

address the need to re-assess exactly what constitutes a reasonable rate of return or a "normal profit," and, although the FCC recognizes new sources of revenues, it does not indicate exactly how it takes these revenues into account in its proposed assessment of USF need.[20] Revenue recovery is a vestige of rate regulation and contrary to what one would expect in a competitive marketplace.

The FCC should not seek to preserve historic levels of net revenues derived from intercarrier compensation.

Reforming intercarrier compensation could lead to reductions in interstate and intrastate access charges and, therefore, in the revenue stream that incumbent local exchange carriers ("ILEC") derive from intercarrier compensation. Offsetting this impact are the following factors: (1) rate reductions will stimulate new demand and thus new revenues; and (2) ILECs will pay less for terminating traffic on other carriers' networks, thus lowering their costs of doing business. Despite these offsetting factors, Rate Counsel recognizes that the net impact of intercarrier compensation reform (*i.e.*, the reduction in revenues relative to the reduction in costs) could yield net revenues for ILECs that are less than historic levels. However, for several reasons, discussed in initial comments and below, it does not then follow that carriers should be "made whole" on a dollar-for-dollar basis. The FCC's erroneous attempt to provide "revenue recovery" leads to flaws in intercarrier compensation reform proposals and universal service reform proposals.

In addition to the SLC increases contemplated by the FNPRM's proposals, the Commission apparently foresees additional increases to end-user charges as evidenced by a proposed referral to the Separations Joint Board "to evaluate the need for any additional

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[20] / *Id.*, at 22.

increases in interstate end-user charges to recover any net loss in interstate and/or intrastate intercarrier compensation revenues as a result of the reform measures" it adopts.[21]

There is not a clear showing that intercarrier compensation reform would prevent carriers from generating adequate returns on their investment.

There is no evidence to suggest that carriers would lack the ability to generate adequate return on investment if intercarrier compensation reform occurs. COMPTEL opposes the proposal put forth by the Organization for the Promotion and Advancement of Small Telecommunications Companies ("OPASTCO") and the Western Telecommunications Alliance ("WTA") (collectively, "OPASTCO and WTA") and incorporated into the Draft Alternative Proposal (in Appendix C), which would provide supplemental Interstate Common Line Support ("ICLS") for rate-of-return carriers because, among other things, "there has been no demonstration that USF compensation is necessary for rate-of-return carriers to meet their authorized rates-of-return."[22] CPUC is concerned about the loss of revenues for small rural carriers and estimates that the ILECs will "lose" $170 million by the end of two-year transition.[23] However, AdHoc Telecommunications Users Committee ("AdHoc") asserts that there is inadequate information about rural carriers' costs and revenues.[24] In any event, Rate Counsel concurs that universal service funding should not be used to compensate carriers for lines and minutes lost to competitors.[25] Comprehensive data is needed before federal and state

[21] / FNPRM, Appendix A, at para. 303 and Appendix C, at para. 298.

[22] / COMPTEL, at 29.

[23] / CPUC, at 14.

[24] / AdHoc, at 6

[25] / COMPTEL, at 30-31; *see also*, Rate Counsel, at 14, 17.

regulators can gauge the impact of reform on carriers' ability to generate a reasonable return on investment, particularly when all sources of revenues are considered.

The Commission should reject proposals to make carriers whole by increasing universal service subsidies and, thus, jeopardizing universal service.

In the proposals under consideration, the Commission provides "escape clauses" for ILECs seeking to be made whole in addition to the proposed SLC cap increases.[26] At the outset, the Commission acknowledges that many companies that receive Universal Service support appear to be doing well, citing the payment of dividends to shareholders, high levels of profitability, and valuations.[27] The Commission states: "In light of these concerns and the mandates of section 254, we agree with commenters that it is not appropriate to require all universal service contributors to pay into the fund so that these carriers can continue to pay dividends."[28] Yet, the proposed solution is simply to make it a little more difficult for carriers to receive *even more* funds, rather than to scrutinize *current* levels of funding. As noted by the Commission, the proposals seek to "ensure that any new universal service subsidies are targeted carefully to situations where they are most crucially needed."[29] After expressing a concern that it should not aim for revenue neutrality and resolving to consider all of a carrier's costs and revenues (regulated and non-regulated),[30] the Commission nonetheless proposes to create a "new

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26 / As noted above, end-user charges (*i.e.* the SLC) may rise even more based on recommendations from the Separations Joint Board.

27 / *See, e.g.*, FNPRM, Appendix A, at para. 312.

28 / *Id. See*, however, Embarq, at 16, stating that "the existence of dividends does not negate the need for universal service support."

29 / FNPRM, Appendix A, at para. 313.

30 / *Id.*, at para. 314.

supplement" to Interstate Access Support ("IAS") and ICLS universal service funding mechanism[31] to "replace" lost intercarrier compensation revenues.[32]

As an initial matter, the Commission restricts the supplemental funding to incumbent carriers because competitors are, by definition, non-dominant and their end-user charges are not subject to state or Commission regulation.[33] As proposed, all carriers (price cap and rate-of-return) must first be charging the maximum level of rates for the Federal SLC, state SLC and retail local service rates permitted under applicable law to be eligible for supplemental funding.[34]

Rate Counsel supports the Commission's conclusion that price cap incumbent LECs who have obtained price deregulation from state regulatory authorities should not be eligible for supplemental funding because they "will be similarly situated to competitive carriers, because without regulation they have the opportunity to recover lost access revenues due to intercarrier compensation reform though increased end-user charges."[35] In addition, the FCC proposes that a price cap incumbent LEC must demonstrate that, after accounting for the increase in end-user charges, as a result of reduced intercarrier charges, the company is still unable to earn a "normal profit."[36] However, the details of the "normal profit" calculation are not determined and, as NASUCA, *et al.* has aptly noted, "the 'devil is in the details,' and the details in the

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31 / *Id.*, at para. 317.

32 / *Id.*, at para. 314.

33 / *Id.*, at para. 318-319.

34 / *Id.*, at para. 315.

35 / *Id.*, at para. 320. *See* Rate Counsel, at 48 stating: "In recent years, many states have deregulated local service, or allowed for rates increases in basic local service, which enables ILECs to set retail rates to recover any foregone implicit subsidies."

36 / FNPRM, Appendix A, at para. 323. The Commission refers to its discussion of normal profit in the *Local Competition First Report and Order*, at para. 699: "total revenue required to cover all the costs of a firm, including its opportunity costs." *Id.*

Chairman's Draft Proposal are seriously undefined . . . "[37] While Rate Counsel commends the Commission for adopting a policy to consider all of the company's costs and revenues that implicate joint use of assets and resources, the practical application of the "normal profit" calculation is ripe for dispute.[38]

Under the Chairman's Draft Proposal, rate-of-return carriers need not make such a showing (*i.e.,* evaluate total costs and total revenues) before receiving additional support,[39] but instead, a rate-of-return carrier may qualify for supplemental funding if it can demonstrate that it would not have "a reasonable opportunity" to earn its authorized rate-of-return.[40] Rate Counsel commends the Commission for its stated decision to refuse to ensure revenue neutrality, but respectfully disagrees that the Commission's plan for supplemental funding is "narrowly targeted"[41] and fully addresses the numerous revenue sources and concerns regarding high dividends, valuations, and margins that the carriers are able to achieve.[42]

Finally, the Draft Alternative Proposal is even more generous to rate-of-return carriers in that it contemplates making carriers whole and perhaps "then some." In the Draft Alternative Proposal, with very little explanation, the Commission finds it "inappropriate" to impose conditions on the receipt of supplemental funding for rate-of-

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37 / NASUCA, *et al.*, at 22.

38 / FNPRM, Appendix A, at para. 324 and footnote 839. The Commission also allows price cap carriers to make a one-way election of rate-of-return regulation. *Id.*

39 / *Id.*, at para. 314.

40 / *Id.*, at para. 322. Of course, as discussed by NASUCA, *et al.*, the 11.25% authorized rate of return is far above reasonable levels and the non-regulated sources of revenues that the Commission purportedly takes into account do not enter the authorized return calculation. NASUCA, *et al.*, at 22. It is also unclear what would constitute a "reasonable opportunity."

41 / FNPRM, Appendix A, at para. 325.

42 / *Id.*, at paras. 312-313.

return carriers[43] and adopts the OPASTCO and WTA proposal, inexplicably finding that "it strikes the proper balance regarding supplemental ICLS support" in that "the only precondition to an incumbent LEC receiving supplemental ICLS support is that the incumbent LEC is under rate-of-return regulation in the interstate jurisdiction."[44] The Commission proposes to adopt the OPASTCO and WTA proposal for two separate components of supplemental ICLS funding. First, rural rate-of-return ILECs would be compensated for all of the revenues lost as a result of any reduction in intercarrier compensation rates that are not recoverable through increased SLCs. Second, rural rate-of-return ILECs that commit to the five-year broadband build-out would be compensated for "unrecoverable revenue losses attributable to losses in access lines and interstate and intrastate minutes of use, using 2008 as a base year."[45] The Commission finds that this "approach" ensures the rate-of-return carriers an "opportunity to recover their authorized rate of return."[46] It also ensures that they are protected from any competitive losses. Rate Counsel agrees with Free Press' description of the OPASTCO and WTA "deal" as "reflect[ing] the worst attributes of an agency that pays more attention to the politics of backroom negotiations and little attention to the guiding statutes."[47]

OPASTCO and WTA urge the Commission to adopt the Draft Alternative Proposal because it contains "the minimum support and protection that rural, rate of return ("RoR")-regulated incumbent local exchange carriers ("ILECs") need to maintain

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43 / FNPRM, Appendix C, at para. 312.

44 / *Id.*, at para. 320.

45 / *Id.*, at para. 321. The second component has a five-year time horizon although the Commission proposed to initiate a proceeding to determine if "modifications are required." *Id.*

46 / *Id.*

47 / Free Press, at 18.

their existing networks and continue to upgrade them for broadband."[48] Yet, OPASTCO and WTA suggest that line losses are occurring "primarily due to customers' elimination of second lines as they subscribe to broadband and population declines in rural areas."[49] The Commission cites evidence that access line losses and declining minutes of use often translate into a broadband line gain, and, that according to an AT&T Annual Report, customers with broadband in additional to basic service are 40% less likely to switch providers and have average revenue of almost 120% more than those without broadband.[50] Rate-of-return carriers likely would have similar results from bundles and revenues derived from non-regulated services. Rate Counsel echoes Free Press' recommendation that the Commission finish the Rural Task Force proceeding[51] in order to determine the actual costs these carriers face and whether there is truly a need for the supplemental funds contemplated by the OPASTCO and WTA proposal.

Despite concluding that the Draft Alternative Proposal appears "to provide a reasonable solution" for rate-of-return carriers, the CPUC states that it "does not support the 'revenue neutrality' concept." [52] Rate Counsel agrees with CPUC's initial analysis that any "recovery" that does occur should be on a "net" basis that takes account of various factors, such as:

> . . . the natural decline in revenue resulting from competition from other communications technologies such as wireless and VoIP. Interstate access revenue has been declining in recent years, and any recovery must take into account the downward trend in ILEC wireline minutes of use and declining line counts. Any federal

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48 / OPASTCO and WTA, at 2.

49 / *Id.*, at 12.

50 / FNPRM, Appendix C, at para. 308 and footnotes 803-804.

51 / Free Press, at 17-18.

52 / CPUC, at 15.

recovery mechanism should reflect these declining revenue trends.[53]

In conclusion, the proposals appear to have been developed in a vacuum wherein the original purpose of the high-cost universal service mechanism has fallen by the wayside. The Commission concludes that the supplemental universal service funding is appropriate "to keep retail rates affordable" but provides absolutely no support for the underlying assumption that retail rates would not be affordable but for the supplemental funding.[54] Rate Counsel agrees with NASUCA et al.'s assessment: "What is missing here, of course, is any connection to the primary purpose of the high-cost USF under federal law: To ensure that rates and service in rural areas – not returns – are reasonably comparable to those in urban areas."[55] The Preamble to the 1996 Act states that the 1996 Act's purpose is: "To promote competition and reduce regulation *in order to secure lower prices and higher quality services for American telecommunications consumers* and encourage the rapid deployment of new telecommunications technologies."[56] And yet, the Commission appears to be shielding the high-cost recipients from the competition that may well lead to lower prices and reduce the need for subsidies.

RBOCs are earning excessive rates of return, which undermines the FCC's concern about potential revenue "shortfalls" resulting from intercarrier compensation reform.

AdHoc express concerns similar to Rate Counsel's long-standing concerns about RBOCs' excessive rates of return on their interstate special access services as well as on

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[53] / *Id.*, at 15-16.

[54] / *See, e.g.,* FNPRM, Appendix C, at para. 313. *See* Rate Counsel, at 43-48 for a discussion of the Commission's continued failure to address the *Qwest II* remand.

[55] / NASUCA, *et al.*, at 23, citing 47 U.S.C. §254(b)(3).

[56] / Emphasis added.

their total company operations.[57] It is hard to fathom that the Commission would allow RBOCs to raise their SLCs while they are earning overall rates of return of 33%.[58]

In assessing the impact of regulatory reform on carriers' ability to generate reasonable returns on their investment in the public network, the FCC should examine all revenues derived from the local loop.

ILECs' comments do not address Rate Counsel's concern that the FCC's proposals fail to account for the billions of dollars that ILECs generate from their basic local loop. It would neither be fair nor result in accurate pricing signals for reform to occur in a vacuum. The fact that carriers are using the local loop, the cost of which has been recovered from consumers, as a springboard for lucrative unregulated services is an essential component of any analysis of "foregone" revenue.

III. INTERCARRIER COMPENSATION

A. THE PROPOSALS ARE FLAWED

The FCC's proposals in Appendix A and C would unlawfully abrogate state rate-making authority.

The FCC floated several trial balloons for intercarrier compensation reform, none of which gained or merited widespread support. Many commenters, for example, concur with Rate Counsel's opposition to the proposal by the FCC to usurp state rate-making authority.[59] Rate Counsel reiterates its previously stated concern that "the Commission

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[57] / Rate Counsel, at 18-20; AdHoc, at 2, 7.

[58] / *See* Rate Counsel, at fn 37, stating: "Total interstate rates of return for AT&T, Qwest and Verizon were 35%, 53%, and 25%, respectively, in 2007. Total RBOC interstate rate of return for 2007 was 33%. FCC, ARMIS Report 43-04, Table 1 (data run November 23, 2008)."

[59] / *See, e.g.*, MDTC, at 8; COMPTEL, at 6-10 (the "Commission has no statutory authority to set rates for intrastate services"); Broadview at 3, 16-29 (describing in detail the lack of legal authority for the Commission to pre-empt state ratemaking over access charges); NASUCA, *et al.*, at 8-9; NARUC, at 6-11; PUCO, at 7 ("The 1996 Act shows that Congress knows it is necessary to expressly override § 152(b) but it has not done so in the context of intrastate access charges").

should not overstep its jurisdictional authority in its efforts to reform intercarrier compensation."[60] To use the interstate SLC to recover "losses" from intrastate rate changes is improper.[61] The Commission should consider the analysis of the National Association of Regulatory Utility Commissioners ("NARUC") that the Chairman's Draft Proposal (Appendix A) and the Draft Alternative Proposal (Appendix C):

> . . . . virtually rewrite key sections of the Statute – overriding literally decades of case law, ignoring express reservations of State authority, and redefining statutory terms in a manner that Congress never intended – to, among other things . . . unlawfully constrain State retail rate design by preempting intrastate access charges, building on the flawed legal rational of the Core Remand order . . . [62]

Rate Counsel concurs with NARUC's assessment that such action by the Commission will not withstand judicial review.[63]

Furthermore, NARUC states that the Commission's methodology in the FNPRM "illegally constrains State retail rate design options and restricts States' ability to set intrastate rates based solely upon State-determined reasonable costs of service."[64] Similarly, WUTC states: "Despite the Commission's efforts to effectively 'federalize' all aspects of intercarrier compensation, the fact remains that state commissions are closest to consumers and the specific aspects of the provision of telecommunications services in their markets, regardless of the means of transmission (circuit-switched or IP)."[65] Rate

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60 / Rate Counsel, at 23. *See, also*, Rate Counsel, at 14-15, 22-23; *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Comments on behalf of the New Jersey Division of the Ratepayer Advocate, May 23, 2005 ("Rate Counsel 2005 ICC Comments"), at 9.

61 / Rate Counsel, at 15.

62 / NARUC, at 4. NARUC also addresses the Commissions' "specious legal rationale" for determining that VoIP services are information services. *Id.* That issue is discussed separately, below.

63 / *Id.*, at 5. NARUC "expect[s] to participate in the inevitable, and likely successful, appeal" of the Core Remand Order. *Id.*, at 6.

64 / *Id.*, at 11 (emphasis and cites omitted).

65/ WUTC, at 4.

Counsel repeats its long-held position that "States are in the best position to assess the affordability of basic services and to examine carrier's need, if any, to adjust rates as a result of modified intercarrier compensation regions. States, similarly, have jurisdiction over intrastate access charges and also are in the best position to design and implement plans for revising those rates."[66]

A multi-year transition to uniform rates is prudent, but states should determine the pace of the transition of intrastate rates.

Several parties raise concerns about the "front-loaded nature"[67] of the reduction of intrastate rates (the initial four-year period).[68] Broadview, *et al.* recommend a five-year transition for reducing intrastate switched access charges to interstate access levels, with 20% reductions occurring in each of the five years.[69] On the other end of the spectrum, Verizon and Verizon Wireless urge the Commission to shorten the transition period and suggest that the current plan "allows for a lengthy and unstructured transition that allows states to postpone uniformity and to permit some carriers to retain their artificially high access rates for ten years."[70] In response to Verizon's and AT&T's advocacy for a more rapid transition to uniform rates (specifically a five-year transition),[71] Embarq supports phased-in proposals to unify intrastate and interstate switched access rates if "provisions

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66 / Rate Counsel 2005 ICC Comments, at 9. *See, also*, Rate Counsel, at 22-23.

67/ *See, e.g.*, WUTC, at 7.

68 / *See* Broadview, *et al.*, at 37, observing that the Stage One reduction of intrastate access charges likely would represent the largest loss of revenues.

69 / *Id.*, at 38.

70 / Verizon and Verizon Wireless, at 42.

71 / AT&T, at 21-22.

are made for reliable revenue recovery mechanisms."[72] Rate Counsel reiterates its view that states, not the FCC, should set the pace for reform of intrastate rates.

Verizon and Verizon Wireless suggest that there is nothing to stop the states from setting an interim rate that is higher than all or most of the access rates of carriers in the state and maintaining that relatively high rate during the glide path until the very end of the period, which would lead to various rates then continuing, with opportunities for arbitrage.[73] Concerns about arbitrage, pumping, and phantom traffic often find themselves to the halls of state regulators, and, therefore, it seems unlikely that states will seek to exacerbate the problem of disparate intercarrier compensation regimes.

Rate Counsel recommends that state regulators, and not the FCC, determine the pace of change to intrastate switched access charges. States not only uniquely possess the rate-making authority to set intrastate access charges, but also, they can seek detailed data and information to guide their decision-making, based on the characteristics of the industry within their jurisdictions.[74] Moreover, Rate Counsel urges the Commission to consider such proposals as that set forth by NASUCA, *et al.*, which would create incentives (rather than mandates) for states to reduce intrastate switched access charges.[75]

The FCC should reject the proposed increases in the SLC caps.

Initial comments do not dissuade Rate Counsel from its strong opposition to increases in the SLC caps. Existing SLCs are now priced below caps in many instances, suggesting that caps are already *above* cost. The proposed caps represent increases of 20

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72 / Embarq, at 24-25.

73 / *See* Verizon and Verizon Wireless, at 46.

74 / *See, e.g.,* Embarq, at 23, referring to its participation in intrastate access charge reform in various states.

75 / NASUCA, *et al.*, at 16-17.

to 25% in the level of caps for residential and business customers and represent increases of even more relative to average SLC rates.[76] There is no justification for the proposed SLC increases,[77] and, furthermore, as proposed by the Commission, the SLC increases would pit business customers against residential customers.[78]

AT&T seeks clarification of the way in which carriers could raise their SLCs, such as when business lines but not residential lines are fully deregulated.[79] Rate Counsel opposes increases in interstate SLCs to recover foregone intrastate revenues. The examples that AT&T offers to demonstrate the potential for ambiguities provide yet further rationale for eliminating those portions of any reform that would usurp state ratemaking authority or that would seek to recover foregone intrastate revenues through increases in interstate charges. Rejecting the proposed increases in the SLC caps similarly would render mood Qwest's concern about the ambiguity of the implementation of the SLC cap increases.[80]

Contrary to the FCC's proposed finding, VoIP is a telecommunications service.

Contrary to the FCC's FNPRM proposed finding that IP-PSTN traffic is an information service, IP-PSTN traffic is telecommunications. NARUC describes the Commission's proposals to classify VoIP services as information services as based on the following: (1) "bare" references to prior orders; (2) faulty reasoning that calls using "net protocol conversion" are thus information services; and (3) "the idea that the FCC can preempt State authority because it is 'inconsistent with [the FCC's] generally

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76 / AdHoc, at 10-11

77 / NASUCA, *et al.*, at 17-21.

78 / AdHoc, at 13.

79 / AT&T, at 39-41.

80 / Qwest, at 5.

unregulated treatment.'"[81] Rate Counsel concurs with NARUC's assessment that the Commission has essentially tried to "shoehorn" fixed VoIP service into the information services classification. NARUC explains:

> Currently, so-called fixed providers of VoIP services are indistinguishable from their PSTN brethren. Their traffic is never part of the so-called public Internet. Their traffic is severable. They interface with the PSTN as do all other carriers. To both end-users and the PSTN, they are indistinguishable from other carriers currently subject to State oversight.[82]

Rate Counsel also concurs with the Massachusetts Department of Telecommunications and Cable ("MDTC") that the proposed determination that VoIP is an information service would cause irreparable harm because, among other things, it would prevent states from protecting consumers, such as safeguarding consumers against billing disputes, disconnection, poor quality E-911, service outages, etc.[83] Furthermore, Rate Counsel agrees with COMPTEL's assessment that the "Commission's classification of IP/PSTN service as an information service is not necessary to implement intercarrier compensation reform and makes no sense."[84]

The classification of VoIP as an information service would jeopardize competitors' interconnection rights.[85] Furthermore, BOCs have stated that voice service provided over their IP-based networks are the same as that provided over their circuit-switched networks.[86] Rate Counsel urges the Commission to heed the opposition of

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81 / NARUC, at 12.

82 / *Id.*, at 13. *See, also*, *id.*, at 13-22.

83 / *See*, e.g., MDTC, at 9-12; NARUC, at footnote 11.

84 / COMPTEL, at 10; Embarq, at 36, indicating that it is "unreasonable and arbitrary" for the FCC to claim that IP/PSTN traffic is enhanced, see *id.*, generally at 35-41.

85 / COMPTEL, at 10-11, 17-19.

86 / *See, e.g., id.*, at 13, quoting Verizon's explanation that its regulated voice service is the same regardless of whether it is provided over fiber or copper loop facilities.

numerous parties that oppose the classification of IP-PSTN traffic as information services.[87] The CPUC recommends that the FCC not render such a decision at this time, but instead focus on intercarrier compensation and USF reform, and that furthermore such a classification could jeopardize the FCC's ability to require contribution from information services.[88] The WUTC states: "Under the FCC's new legal theory, what was once a 'dual-based' jurisdictional approach to regulating telecommunications services (i.e., Commission regulation of interstate and state commission regulation of intrastate services) has now become a regime in which the Commission proscribes the regulations applying to both interstate and intrastate services with states left to implement only those matters that Commission deems appropriate."[89] The Public Utilities Commission of Ohio ("PUCO") asserts that the FCC "takes the unnecessary and unlawful step of declaring that all PSTN services either originating or terminating over Internet Protocol (IP) are 'information services.'"[90]

Verizon and Verizon Wireless express concern that VoIP and IP-enabled services will be handicapped if subject to "more than 50 different sets of rules" if the states have jurisdiction,[91] yet also ask the Commission to confirm that these carriers have interconnection rights, including the right to use state arbitration processes to resolve interconnection disputes.[92] Verizon and Verizon Wireless assert that the Commission's

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87/ *See also*, Broadview, *et al.*, at 13; NASUCA, *et al.*, at 8-9; Qwest, at 15 (stating that "as a policy matter, it makes no sense to treat IP/PSTN traffic any differently than any other traffic on the PSTN"); NARUC, at 11-22.

88/ CPUC, at 5-6.

89/ WUTC, at 4.

90/ PUCO, at 8-9, cite omitted (see generally, 8-12).

91/ Verizon and Verizon Wireless, at 2.

92/ *Id.*, at 3. See, also, *id.*, at 27.

ability to address E911, CPNI, LNP, and universal service issues will not be affected by classification as information services.[93]

Rate Counsel disagrees with Verizon and also with AT&T's view[94] that all fixed or nomadic VoIP services that are capable of interconnecting with the public switched telephone network are information services. The Commission should heed NARUC's concern that functionally equivalent services should be afforded similar regulatory treatment and that "an approach that treats services that are substitutable for/functionally equivalent to existing telephony service differently is inconsistent with Congressional intent . . ."[95] States are in the best position to protect consumers and to provide the appropriate oversight of fixed VoIP services, which clearly are telecommunications, and not information service, and which provide intrastate functionality.

The FCC should resolve the long-brewing issue of phantom traffic.

Initial comments, in contrast to the reaction regarding the proposals as a whole, show widespread support for resolving phantom traffic.[96] Rate Counsel reiterates its support for measures that would prevent carriers from shirking their responsibility to contribute to the cost of the public network. Carriers should be required to include information identifying call origin on all calls and should be prohibited from disguising or mis-identifying terminating traffic. As described by Broadview, *et al.*, the proposed rule changes "would effectively prohibit any altering or stripping of SS7 CPN, MF ANI

93/ *Id.*, at 24-25.

94/ AT&T, at 23.

95/ NARUC, at 24.

96/ *See, e.g.*, Broadview, *et al.*, at 2, 7-8, 29-35; CPUC, at 17; NASUCA, *et al.*, at 23; Qwest, at 20; Verizon and Verizon Wireless, at 5; Embarq, at 5, at 29 (indicating that the Act does not give the FCC carte blanche to preempt states on regulation of rates for intrastate traffic), at 29-35 (for general discussion.).

or CN signaling information and obligate intermediate service providers to pass, unaltered, whatever signaling information they receive."[97]

Although Qwest supports addressing phantom traffic in a way generally similar to that set forth in the FCC's FNPRM, it also asserts that the FCC's proposal "goes well beyond what that industry consensus plan requested" by imposing "potentially broad new obligations on transit service providers, requiring them to pay the 'highest applicable' rate for termination for certain traffic when another carrier fails to meet certain obligations."[98] Qwest recommends that the Commission eliminate that provision of the phantom traffic solution because it does not address the difficulty that transit service providers have in obtaining compensation for their services,[99] and if the Commission does not eliminate the provision, that it clarify the regulatory status of transit services.[100] As explained by Qwest, transit service providers cannot prevent others from delivering traffic to them, and yet, have little recourse if the originating carriers fail to compensate them.[101] Qwest observes that "the proposed termination expense transfer provision is quite like throwing lighter fluid on an already smoldering fire" because it would put transit service providers "entirely at the mercy of both originating and terminating carriers and into the middle of their disputes."[102] Rate Counsel recommends that any

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97 / Broadview, *et al.*, at 7-8, citing FNPRM, Appendix A, at paras. 330-333.

98 / Qwest, at 20.

99 / *Id.*, at 22, 26-27. Transit services are those that occur when an intermediate carrier, which does not have a relationship with the end user, transports traffic received from the calling party's carrier to the terminating carrier (which, in turn, has the customer relationship with the called party). *Id.*, at 23.

100 / *Id.*, at 27-28.

101 / *Id.*, at 23.

102 / *Id.*, at 26-27.

final rules issued that are intended to address phantom traffic remove any lingering uncertainty about payment obligations.

Rate Counsel concurs with AT&T that measures should be taken to discourage traffic-pumping schemes.[103] AT&T supports signaling requirements to discourage phantom traffic, and recommends that the Commission prohibit terminating carriers from varying their compensation structure on a call-by-call basis (where they charge the ultimately responsible carrier for some calls and the transit carrier for other calls).[104]

The Commission should not hold the matter of phantom traffic hostage to the more complex matters relating to intercarrier compensation and universal service reform,[105] but rather should adopt rules in a timely manner that require all calls to include the requisite call signaling information.

B. COST STANDARD

The FCC's proposed cost standard is ill-conceived and should be abandoned.

Others echo Rate Counsel's criticisms of the FCC's proposed use of a new marginal cost standard to replace total element long run incremental cost ("TELRIC") in setting rates for intercarrier compensation.[106] As proposed, intercarrier compensation rates would be based on calculations that lacks common costs and, yet, in sharp contrast, SLC rates would exceed significantly fully distributed costs.[107]

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103 / AT&T, at 32-34.

104 / *Id.*, at 35-37.

105 / Other commenters agree. *See, e.g,.* Verizon and Verizon Wireless, at 64 stating that the phantom traffic portions of the proposed plan "could be adopted on a standalone basis."

106 / *See, e.g.*, Rate Counsel, at 27-29; NASUCA, *et al.*, at 9-16; Embarq, at 4.

107 / AdHoc, at 8-9.

Rate Counsel disagrees with AT&T's position that the FCC's proposed cost standard is superior to TELRIC as the basis for setting intercarrier compensation rates.[108] Among other reasons that AT&T offers in support of the FCC's new proposed cost standard is that it will push costs onto carriers' end users, thereby "reward[ing] efficient carriers and punish[ing] inefficient ones" by forcing carriers to recover common costs from their end users in retail rates.[109] Contrary to AT&T's arguments, shifting yet more cost recovery to the end user is not a desirable goal nor would the proposed change be more economically efficient. Joint and common costs are real costs that must be incurred in order to enable a carrier to terminate traffic. Including a fair share of these costs in the rates set for intercarrier compensation, therefore, results in an accurate pricing signal. Embarq echoes the concern raised by Rate Counsel that failure to assign and allocate common cost to access charges could result in higher end user charges. Embarq states: "By removing any contribution toward common costs from the 'additional cost' standard, the proposed order would require that other services recover more than a reasonable allocation of common costs."[110] Embarq explains further:

> If the implication is that such a fixed fee would be recovered from end-users, the effect of this would be to place a disproportionate share of common costs on those users. And there is no economic justification as to why it is either desirable or efficient to have end-users to pay a greater share of common costs just so carriers sending terminating traffic can pay a smaller share of common costs.[111]

108/ AT&T, at 9-14.

109/ *Id.*, at 11.

110/ Embarq, at 44.

111/ *Id.*, at 46.

Rate Counsel reiterates its opposition to the Commission's departure from its long-standing use of TELRIC as the basis for setting intercarrier compensation rates. Such a major and hastily considered change would be unnecessary, yield misleading pricing signals, and yield an internally inconsistent costing regime whereby some rates (*i.e.*, those for intercarrier compensation) are based on costs that lack any assignment and allocation of common costs, and other rates (*i.e.*, those for unbundled network elements) would recover common costs. Such a result would be nonsensical, anticompetitive, and likely shift yet more cost recovery improperly to consumers.

IV. UNIVERSAL SERVICE REFORM

The elimination of the identical support rule is an important step in reducing the burden of the universal service fund on consumers.

As discussed in initial comments, the FCC should eliminate the identical support rule.[112] Consumers should not subsidize more than one carrier in areas that require support. Rate Counsel continues to urge the Commission to adopt the phase-down in the Draft Alternative Proposal (Appendix C) and to shift any funds "saved" to a broadband fund separate from this high-cost fund.[113] As noted by the Commissioners, there is general support for the elimination of the identical support rule.[114]

112/ Rate Counsel, at 42-43.

113/ *Id.*

114/ FNPRM, Joint Statement of Commissioner Michael J. Copps, Jonathan S. Adelstein, Deborah Taylor Tate and Robert M. McDowell, Re: *High-Cost Universal Service Support*, WC Docket No. 05-337; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45; *Lifeline and Link Up*, WC Docket No. 03-109; *Universal Service Contribution Methodology*, WC Docket No. 06-122; *Numbering Resource Optimization*, CC Docket No. 99-200; *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98; *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92; *Intercarrier Compensation for ISP-Bound Traffic*, CC Docket No. 99-68; *IP-Enabled Services*, WC Docket No. 04-36, November 5, 2008. *See, also*, NASUCA, *et al.*, at 38-39; Verizon and Verizon Wireless, at 3 and 28.

COMPTEL raises the concern that the elimination of support for competitive eligible telecommunications carriers ("CETC") would discourage carriers other than the ILEC from serving high cost areas, thus "depriving customers of a choice of carriers and services."[115] Rate Counsel welcomes choice and competition for consumers but opposes expensive efforts to prop up competition that is not, but for subsidies, economically sustainable. If support is needed to enable a single carrier to serve a customer, it would be an imprudent use of societal resources to prop up two or more networks simply to give consumers a choice. On the other hand, Rate Counsel does not presuppose that the ILEC is the most efficient supplier of service in high cost areas. Therefore Rate Counsel supports the use of a reverse auction on a pilot basis to assess the feasibility of this mechanism for identifying and supporting the most efficient provider.

Verizon and Verizon Wireless also back the phase-down of support for all CETCs over five years,[116] *something that is required of Verizon Wireless as a condition of its merger with ALLTEL.*[117] In this proceeding, Verizon and Verizon Wireless claim that the phase-down of support for all CETCs is "critical to create a level playing field" among all CETCs.[118] Of course, the point of the phase-down commitment of the merger is an acknowledgement that Verizon Wireless and ALLTEL are different, as described by the Commission:

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115 / COMPTEL, at 24.

116 / Verizon and Verizon Wireless, at 3.

117 / *In the Matter of Applications of Cellco Partnership d/b/a Verizon Wireless and Atlantis Holdings LLC; For Consent to Transfer Control of Licenses, Authorizations, and Spectrum Manager and De Facto Transfer Leasing Arrangements; and Petition for Declaratory Ruling that the Transaction is Consistent with Section 310(b)(4) of the Communications Act*, WT Docket No. 08-95; File Nos. 0003463892, et al., ITC-T/C-20080613-00270, et al.; File No. ISP-PDR-20080613-00012, *Memorandum Opinion and Order and Declaratory Ruling*, rel. November 10, 2008, at para. 197.

118 / Verizon and Verizon Wireless, at 4. Not surprisingly, Verizon and Verizon Wireless do not support the proposal in Appendix A to allow CETCs to receive support based on their own costs as compared to benchmarks. *Id.*, at 29.

> The proposed transaction constitutes a merger of the largest wireless company in the United States, based on revenues, as well as the number of retail customers, with another wireless company that is the largest recipient of the high-cost competitive ETC support. Such unique facts and large scope of this transaction compel us to condition our approval of the proposed transaction on Verizon Wireless's commitment to phase down its competitive ETC high cost support over five years, as discussed herein. In light of Verizon Wireless's voluntary commitment, we decline to impose a condition that, prior to receipt of such funding, Verizon Wireless demonstrate costs of providing universal service. We find that Verizon Wireless's voluntary commitment to phase down competitive ETC high cost support over five years is sufficient to relieve commenters' concerns. We also note that the Commission is currently considering this issue, along with others, in a rulemaking on comprehensive high-cost universal service reform.[119]

Rate Counsel disagrees with Verizon and Verizon Wireless that it is somehow unfair to treat other CETCs differently. After all, the point of the merger commitment was that the Commission recognized that the merged companies would be different.

Rate Counsel does, however, support Verizon and Verizon Wireless' proposal (much like the Joint Board's recommendation and Rate Counsel's prior comments) to use the savings from the phase-down of CETC funding for new infrastructure. Specifically, Verizon and Verizon Wireless urge the Commission to open a rulemaking "to examine whether and how it could use some of the savings for a new infrastructure fund for one time grants, not ongoing subsidies, to encourage network build-out of both wireless and broadband facilities into unserved areas. Targeting funds to areas where broadband or

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[119] / *In the Matter of Applications of Cellco Partnership d/b/a Verizon Wireless and Atlantis Holdings LLC; For Consent to Transfer Control of Licenses, Authorizations, and Spectrum Manager and De Facto Transfer Leasing Arrangements; and Petition for Declaratory Ruling that the Transaction is Consistent with Section 310(b)(4) of the Communications Act*, WT Docket No. 08-95; File Nos. 0003463892, et al., ITC-T/C-20080613-00270, et al.; File No. ISP-PDR-20080613-00012, *Memorandum Opinion and Order and Declaratory Ruling*, rel. November 10, 2008, at para. 197.

wireless services are not yet available could further the universal service goals of the Act."[120] Rate Counsel urges the Commission to give this proposal serious consideration.

As proposed, the "revenue recovery opportunities" are ill-advised.

Qwest raises the concern that although rate-of-return LECs would be guaranteed to be made whole,[121] price cap carriers would be unlikely to be able to benefit from any new USF because they would have to meet the more stringent showing of an inability to make a "normal profit" across all operations.[122] Rate Counsel continues to have a different concern, namely that the FCC should not establish any new USF without first responding to the *Qwest II* remand.[123]

Rate Counsel also recognizes the unique situation of mid-sized ILECs (for example, mid-sized ILECs benefit less from access charge reductions than do the large ILECs because they are not integrated with purchasers of access service (interexchange and wireless carriers)),[124] but the SLC increases and IAS and ICLS that they seek,[125] should not be considered an entitlement. Instead, carriers, regardless of whether they are rate-of-return or price cap, and regardless of their size, should be required to demonstrate a need for subisides and be held accountable for any USF support they receive.

Comments suggest that too many questions still remain concerning the implementation of the numbers-based contribution mechanism for implementation at this time.

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120 / Verizon and Verizon Wireless, at 31.

121 / Qwest describes the "remarkably generous revenue recovery for rate-of-return ILECs through access to a supplemental Interstate Common Line Support ('ICLS') fund." Qwest, at 10.

122 / *Id.*, at 8.

123 / *See* discussion of *Qwest II* at Rate Counsel, at 42-48.

124 / Embarq, at 6.

125 / *Id.*, at 7.

Rate Counsel continues to oppose a numbers-based system for determining contributions as do others.[126] MDTC expresses concern about the insufficient data upon which the proposal is based.[127] Still others highlight the incomplete nature of the current proposal. Even those that do not necessarily oppose a numbers- or connections-based assessment highlight the numerous unanswered questions and complexities.[128] For example, CPUC expresses concern that Appendix A fails to describe how wireless numbers would be treated and that wireless providers take the position that they don't have "residential" and "business" customers, but just provide wireless service.[129] Despite supporting the numbers-based system for its supposed simplicity, Verizon and Verizon Wireless disagree with the Commission's proposed used of "assessable numbers" arguing that it is extremely problematic[130] highlight several aspects of the proposal as being complex.[131] Although Qwest supports a numbers-based system, its comments demonstrate that there would be many time-consuming steps to change over the contribution methodology and that there are ambiguities relating to the split between assessable numbers and assessable connections.[132] Furthermore, Qwest proposes that carriers be able to recover the cost of developing and deploying a new contribution methodology from end users in a manner similar to the local number portability charge

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126 / See Rate Counsel, at 48-49; NASUCA et al., at 39-41; Pennsylvania Public Utility Commission, at 15.

127 / MDTC, at 25-26; Rate Counsel, at 49.

128 / CPUC, at 12-13; Broadview, *et al.*, at 54-56; Citynet, LLC, Granite Telecommunications, Inc., Paetec Communications, Inc., RCN Telecom Services, Inc. and U.S. TelePacific Corp., at 27; Public Service Commission of Wisconsin, at 4; Embarq, at 17-19.

129 / CPUC, at 13; *see also* Broadview, *et al,* at 54-56, describing various complexities of the proposals.

130 / Verizon and Verizon Wireless, at 34.

131 / *Id.,* at 34-36.

132 / See steps delineated by Qwest, at 42-43.

recovery.[133] Rate Counsel opposes such a recovery, which would further burden consumers. Rate Counsel agrees with Embarq that reforming the contribution mechanism is less important than reforming the distribution of USF.[134]

The Appendix B proposal, which is based on the *ex parte* filed by AT&T and Verizon on October 20, 2008, would establish assessable connection charges of $5.00 per month for connections up to 64 kbps and $35.00 per month for assessable connections over 64 kbps. COMPTEL provides compelling examples of how the Commission's proposal in Appendix B would harm small businesses.[135] A customer that pays $155 per month for a DS1 would experience an increase in its monthly USF fee from $17.67 (i.e. assuming a 11.4% USF fee) to $35 (plus increases do to assessable number charges and increases in the SLCs). A customer with eight 64 kpbs voice lines would pay connection charges of $40 per month whereas a business customer that has an OC-48 would pay a connection charge of only $35 per month.[136] According to COMPTEL, the connections-based proposal would lead to a substantial reduction in USF fees for large enterprise customers and to substantial USF fee increases for small business customers.[137]

Contrary to the assertions of OPASTCO and WTA, universal service is not threatened by the unpredictable nature of end-user charges.[138] Rate Counsel continues to support NASUCA in its assessment that a revenue-based assessment is "more robust and equitable" than the proposed numbers-based methodology, and although the Lifeline

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133 / Qwest, at 43.

134 / Embarq, at 17.

135 / COMPTEL, at 25-27.

136 / *Id.*, at 26.

137 / *Id.*

138 / OPASTCO and WTA, at 7. *See, also,* Verizon and Verizon Wireless, at 4 and 34.

exemption is commendable, the proposal fails to address the budget constraints of many low-use households not covered by Lifeline.[139]

Reverse auctions should only be used on a pilot basis at this juncture.

Reverse auctions have a host of problems discussed in detail in Rate Counsel's initial comments and in comments earlier this year,[140] Based on its review of others' initial comments, Rate Counsel continues to support the use of reverse auctions only on a limited or trial basis. Furthermore, Rate Counsel remains concerned about the not so unlikely outcome of the absence of a bidder in reverse auctions.[141] However, Rate Counsel is opposed to OPASTCO and WTA's proposed solution: providing the incumbent with a yet higher level of support.[142] OPASTCO and WTA incorrectly conclude that if no provider bids at the set reserve price (*i.e.*, the current level of support) "it is a clear indication that the rural ILEC's existing support amount is inadequate for *any* carrier to be capable of providing broadband to 100 percent of the customer locations within the study area."[143] This logic is faulty for a number of reasons. First, a carrier not already operating in the area may indeed face higher sunk costs to deploy a network. The assumption that the current incumbent does not have enough support to incrementally provide broadband is neither proven nor disproven by the alternative providers' failure to bid at the reserve price. Second, the failure of the auctions to produce bidders is more likely to be the result of an artificial linkage between high-cost support (and thus the imposed provider of last resort obligations) and broadband deployment. There is no

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139 / Rate Counsel, at 49.

140 / *Id.*, at 38-42; Rate Counsel April 2008 USF Comments, at 10, 57.

141 / Rate Counsel, at 41.

142 / OPASTCO and WTA, at 24-25.

143 / *Id.*, at 24.

evidence that the most efficient way to deploy broadband is to do so by tying deployment to all the other services required of an ETC plus the provider of last resort and comparable price requirements. The most inexpensive, efficient broadband providers may have no interest in taking on all of the requirements of an ETC. As discussed in initial comments, the Commission should investigate all broadband solutions and "[a]ny broadband subsidies should be directed to the most efficient technology . . . "[144]

The Commission should be commended for capping the high-cost fund, but has failed to address the continued problems with the high-cost fund and the current proposals simply perpetuate those problems.

As stated in initial comments, Rate Counsel views the Commission's proposed cap of the high-cost fund as only a necessary first step in reforming the high-cost fund, and furthermore, is extremely troubled by the Commission's apparent disregard for the serious shortcomings highlighted and addressed by the Joint Board and the Courts that remain unaddressed.[145] Rate Counsel disagrees with commenters that describe the cap as arbitrary and that express concern that capping the fund will harm providers.[146] There is no evidence that costs should necessarily be increasing every year. As such, the cap can be viewed as a compromise in that many carriers are likely receiving more subsidies than they require (*i.e.*, even capped, the high-cost fund may be too large). Rate Counsel agrees with CPUC's observation that a "permanent cap will simply fix in place the flaws

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144 / Rate Counsel, at 42.

145 / *Id.*, at 32-33. *See*, also WUTC, at 6. Until the Commission addresses whether the level of support is adequate to provide for reasonably comparable and affordable rates (the subject of the *Qwest II* remand), it cannot adequately address assertions, such as WUTC's, that "without sufficient support, both affordability and service quality are put at risk in [rural] areas." *Id.*, at 7.

146 / *See*, e.g., CPUC, at 9. OPASTCO and WTA express concern about rate-of-return ILECs after 2010 when support is frozen, stating that such support "will no longer be adequate to recover increased network cost (such as those for future broadband upgrades) nor will it be adequate to provide the opportunity to earn the rate of return authorized by the Commission." OPASTCO and WTA, at 13.

inherent in the current system" but contrary to CPUC, believes that the cap is a step in the right direction.[147]

Furthermore, the Commission proposed to add broadband deployment as an additional element, further straining the high-cost fund while ignoring whole areas of the country.[148] Rate Counsel continues to support the sunset of the non-rural high-cost fund and high-cost support for Bell operating companies and urges the FCC to reconsider its proposal to combine the broadband and provider of last resort funds (after rejecting, without explanation, the separate funds proposed by the Joint Board), which makes a targeted approach to broadband funding more difficult and "would contribute to the unending USF entitlement program for carriers."[149] As discussed in more detail below, funds for broadband deployment are more appropriately implemented as one-time or short-term grants for deployment, which is one of the myriad of reasons that the high-cost fund is a poor fit.[150]

The linkage of broadband deployment to high-cost funds may have unintended consequences.

Like Rate Counsel, many commenters warn that tying broadband deployment requirements to high-cost funds may have unintended consequences.[151] Although some opposition to broadband deployment requirements and particularly estimates of the additional cost of deployment may be exaggerated, there may indeed be particular hard-

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147 / CPUC, at 10.

148 / Rate Counsel, at 32-33, 36.

149 / *Id.*, at 34-35. PUCO similarly advocates separate USF funds to support the different goals of ubiquitous voice telephone service and ubiquitous broadband availability. PUCO, at 22. *See also, id.*, at 29 stating that the FCC should not try another "one size fits all" solution because "one size never really fits all."

150 / *See, also,* Qwest at 39 and footnote 62.

151 / Rate Counsel, at 37; NASUCA, *et al.*, at 24-28; WUTC, at 6; CPUC, at 11.

to-serve areas that cannot be reached under the current high-cost program. CPUC describes the 100% deployment requirement as "draconian" particularly with respect to rural carriers.[152] WUTC expresses concern that the deployment requirements may actually deter investment: if carriers cannot deploy to 100% of customers they may just cease any additional investment and the Commission's proposals "run the risk of implementing a cure for maladies that actually kill the patient."[153]

Finally, the funds that would be included in the high-cost/broadband deployment program are of such a magnitude that it is doubtful that the political will would exist to target additional funds to the areas that lack broadband but that are not in designated high-cost study areas. The insufficient sum proposed for the Lifeline Pilot Program is one example, discussed in more detail below.

Verizon and Verizon Wireless state that the "first priority for the Commission in this proceeding is to get the rules right for the services of the future: broadband and IP-based services."[154] While Rate Counsel disagrees with Verizon and Verizon Wireless about what those rules should be, Rate Counsel agrees with the premise. The Commission should refrain from addressing broadband deployment by simply inserting it into a broken high-cost support system.

There should be a separate broadband fund with states responsible for administering funds.

The FCC should establish a separate broadband fund, with state administration.[155] The FCC's current proposals would do little to address the numerous areas in the country

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152 / CPUC, at 11.

153 / WUTC, at 6.

154/ Verizon and Verizon Wireless, at 1.

155 / *See, e.g.,* MDTC, at 22-23; NASUCA, *et al.*, at 28.

that are not designated as high-cost, yet where consumers lack broadband access.[156] Rate Counsel agrees with Qwest that the Commission's broadband program should have "clear, realistic goals and performance measures" and that a broadband program should provide one-time grants for applicants to deploy broadband to unserved areas.[157]

The FCC should explore and support alternative broadband technologies.

Based on its review of initial comments, Rate Counsel continues to support pilot trials of diverse broadband technologies so that the FCC, working in collaboration with states, can identify the most cost-effective ways of bringing broadband access to unserved and underserved areas in the country. For example, the FCC should explore broadband over powerline and WiMAX.

On November 4, 2008, the FCC approved the transfer of control of licenses held by Sprint Nextel and by Clearwire Corporation to the New Clearwire Corporation. Sprint Nextel will obtain 51 percent ownership in New Clearwire.[158] The merger of the two companies is part of an effort to deploy a nationwide WiMAX-based network.[159] The

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156 / NASUCA, *et al.*, at 25-27.

157 / Qwest, at 39, and fn 62.

158 / *In the Matter of Sprint Nextel Corporation and Clearwire Corporation; Application for Consent to Transfer Control of Licenses, Leases, and Authorizations*, WT Docket No. 08-94, Files Nos. 0003462540 *et al.*, *Memorandum Opinion and Order*, rel. November 7, 2008, at para. 1.

159/ As described by one source: "WiMax is the industry term for a long-range wireless networking standard. WiMax techology has the potential to deliver high-speed Internet access to rural areas and other locations not serviced by cable or DSL technology. WiMax also offers an alternative to satellite Internet services. WiMax technology is based on the IEEE 802.16 WAN communications standard. WiMax signals can function over a distance of several miles / kilometers. Data rates for WiMax can reach up to 75 megabits per second (Mb/s). A number of wireless signaling options exist ranging anywhere from the 2 GHz range up to 66 GHz. WiMax equipment exists in two forms. WiMax base stations are installed by service providers to deploy the technology in a coverage area. WiMax antennas must be installed at the home or other receiving location. As WiMax evolves, these antennas will change from being mounted outdoors, to smaller varieties set up indoors, and then finally to built-in versions integrated inside mobile computers. Similar to other types of Internet access, consumers will subscribe and pay a recurring fee to connect to the Internet via WiMax. WiMax is developed by an industry consortium, overseen by a group called the WiMax Forum. The WiMax Forum certifies WiMax equipment to ensure it meets the technology standards. WiMax is not a replacement for Wi-Fi hotspot and home networking technologies primarily for

FCC described the deployment of the proposed network as leading to "increased competition, greater consumer choice and new, innovative wireless services."[160]

The FCC should modify its proposed Broadband Lifeline Pilot.

Various parties make compelling cases for the Commission to refine its Broadband Lifeline Pilot.[161] Rate Counsel fully supports broadband subsidies for Lifeline customers and urges the Commission to issue a separate notice of proposed rulemaking, based in part on the comments filed in this proceeding, to establish rules for such a program.

Verizon and Verizon Wireless urge the Commission to better determine the details of its Lifeline Pilot in another NPRM. "As proposed in the draft orders, the Lifeline and Link-Up broadband program is impractical and places all of the administrative burden on carriers, which provides a disincentive for ETCs to participate."[162] In terms of being impractical, Verizon and Verizon Wireless note that the "first come, first served" aspect is questionable in that it means that a customer can place an order but the customer and the provider will not know whether the service will be subsidized.[163]

A ten-dollar broadband subsidy is inadequate.

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cost reasons. Also Known As: Worldwide Interoperability for Microwave Access." *See* http://compnetworking.about.com/od/wirelessinternet/g/bldef_wimax.htm.

160/ FCC News Release, "FCC Approves, with Conditions, Sprint-Nextel/Clearwire Transaction," November 4, 2008. The approval is conditioned upon Sprint Nextel's commitment to phase out requests for federal high-cost universal support over five years and to adopt a wireless E911 location accuracy compliance measurement on a county basis.

161 / *See* MDTC, at 27; NASUCA, *et al.*, at 32-37.

162 / Verizon and Verizon Wireless, at 32.

163 / *Id.*, at footnote 37.

Rate Counsel concurs with Qwest that, among other things, the Commission analyze existing broadband rates in order to determine the level of support that would yield affordable access for low-income households.[164] Indeed, the proposed $10 per month subsidy may be insufficient to enable low-income households to subscribe to broadband Internet access.

As Table 1 shows, the least expensive DSL plans offered by AT&T, Qwest, and Verizon range between $19.95 and $49.99 per month. Cable companies' broadband offerings range in price between $29.95 and $57.95 per month. Furthermore the lowest rate available for broadband service is tied to the purchase of other services. For example, the $29.95 cable Internet access service offered by Cablevision requires purchase of the entire "Triple Pack" – Internet, television, and telephone service. Similarly, the lowest-priced Internet service from Qwest requires purchase of a particular level of local phone service.

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164 / Qwest, at 40.

Table 1

Representative Lowest-Priced Broadband Offers[165]
(sorted by rate)

Service Provider	Download Speed	Rate per Month	Notes
AT&T	768 kbps	$19.95	
Verizon	1 Mbps	$19.99	
Cablevision	15 Mbps	$29.95	Promotional offer; customer must order Triple Pack.
Time Warner Cable	5 Mbps	$29.95	Offer good for first six months only.
Qwest	1.5 Mbps	$29.99	Offer good only for new customers purchasing certain local phone packages.
Comcast	12 Mbps	$42.95	Requires package.
Cox	9 Mbps	$44.95	

An assessment on all broadband revenues should be used to support broadband subsidies.

In its June comments, Rate Counsel proposed that an assessment on broadband services be used to support broadband subsidies for Lifeline participants.[166] NASUCA similarly supports such an assessment.[167]

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165 / Sources: http://www22.verizon.com/Residential/HighSpeedInternet/Plans/Plans.htm, http://www.att.com/gen/general?pid=10891, https://myaccount.qwest.com/qcms/qCmsRepository/Promotions/Broadband/PromotionalText/Popups/SilverPricing.html, http://www.comcast.com/Shop/Buyflow/Default.ashx?SourcePage=Internet, http://www.optimum.com/online/index.jsp, http://www.coxspecials.com/3/?cid=53247&affid=cideals-BBI&, http://www.roadrunneroffers.com/16/premium.php?id=622.

166 / *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *High-Cost Universal Service Support*, WC Docket No. 05-337, Reply Comments of the New Jersey Division of Rate Counsel, June 2, 2008 ("Rate Counsel June 2008 USF Reply Comments"), at 7, 37-38.

167 / *See, e.g.*, NASUCA, *et al.*, at 29.

In its April comments, Rate Counsel estimated that the three BOCs generate as much as $18 billion annually in DSL revenues.[168] Because this preliminary analysis was limited to only the three BOCs, it significantly underestimated industry-wide broadband revenues. For example, based on the FCC's most recent high speed Internet access report, there are more cable modem service subscribers than DSL subscribers in the United States.[169] In June, Rate Counsel extended the analysis presented in initial comments to include those non-RBOCs providing DSL services, as well as companies providing cable-based access.[170] Table 2 includes Rate Counsel's estimate that in 2007, the industry-wide revenue from broadband was between $12 billion and $44 billion.[171]

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168 / *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *High-Cost Universal Service Support*, WC Docket No. 05-337, Comments of the New Jersey Division of Rate Counsel, April 17, 2008 ("Rate Counsel April 2008 USF Comments"), at 30. *See* Table 5 showing an estimated range spanning $5 billion to $18 billion.

169 / See Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, *High-Speed Services for Internet Access: Status as of June 30, 2007*, March 2008, at Table 1, which shows approximately 27.5 million DSL subscribers and 34.4 million cable modem subscribers as of June 2007.

170 / Rate Counsel June 2008 USF Reply Comments, at 35-37.

171 / The estimates span a wide range because consumers may pay a wide range of prices, which, in turn, affects the calculation of the total revenues. In Table 2, the "low" estimate corresponds with a range of monthly rates between $12.99 and $26.99, and the "high" estimate corresponds with a range of monthly rates between $54.99 and $64.99. Note that Rate Counsel has used the pricing data available in April 2008 presented in the earlier round of comments and does not update this analysis based on the rates in Table 1 above. Of course, to the extent that rates are now higher, broadband revenues would also be higher.

Table 2

Estimate of Broadband Revenues – 2007

	Number of Connections	Estimated 2007 Revenues Low Estimate	High Estimate
RBOC DSL	25,432,000	$4,897,088,160	$18,000,245,040
Non-RBOC DSL	2,084,171	$401,319,956	$1,475,133,246
Cable	34,408,553	$6,625,578,700	$24,353,664,103
Total	61,924,724	$11,923,986,816	$43,829,042,389

Note: This estimate of revenues from broadband extends earlier analysis of RBOC (AT&T, Verizon, and Qwest) broadband revenues. (See Rate Counsel Initial Comments at Table 5.) Using the results of the earlier analysis, the revenue per connection is applied to the non-RBOC DSL connections and the cable-modem connections, neither of which were included in the previous analysis. Total DSL and cable-modem connections are as reported by the FCC.

Sources: Websites for AT&T, Qwest, and Verizon, visited 4/10/2008; AT&T 4Q 2007 Investor Briefing; Qwest Historical Financial Information As of December 31, 2007; Verizon Investor Quarterly 4Q 2007; FCC, High Speed Services for Internet Access: Status as of June 30, 2007, Table 1.

Rate Counsel recommends that the FCC assess a broadband USF surcharge on broadband providers for the specific and limited purposed of subsidizing (1) one-time construction charges for deploying broadband in unserved areas and (2) broadband Lifeline support. A small surcharge, applied to such a large base of revenues, would assist the Commission in ensuring that all Americans have access to affordable broadband service. States could be required to provide matching funds.

V. CONCLUSION

Rate Counsel urges the Commission to consider the numerous compelling reasons set forth in initial comments for rejecting the proposals for intercarrier compensation and universal service reform. The Commission should, however, address phantom traffic in a timely manner, eliminate the identical support rule and focus soon thereafter on establishing broadband subsidies for Lifeline participants. Furthermore, the Commission should base any proposals on federal-state cooperation, whereby the Commission does not seek to pre-empt state rate-making authority, and where new programs, such as those involving broadband deployment, are administered by states.

Respectfully submitted,

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